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SUBJECT: BUILDING BETTER IRAQI OIL CONTRACTING PERSONNEL

Classified By: Classified By: Acting Economic Counselor Ruth Hall, Reas
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¶1. (C) Summary: From March 29 to April 2, the Department of Commerce's Commercial Law Development Program (CLDP) held a four day workshop for Ministry of Oil (MoO) personnel on negotiating and contracting with International Oil Companies (IOC). Dr. Sabah Al-Saidi, senior legal advisor to the Petroleum Contracts and Licensing Directorate (PCLD), led the MoO participants, who came from PCLD, the two main operating North and South Oil Companies, and representatives of various directorates active in contracting within the MoO. The MoO participants included accountants, lawyers, and petroleum experts. Two U.S. law professors with extensive oil related experience and a U.S. Lawyer with prior experience in the Iraqi hydrocarbons sector provided the instruction, which covered the basics of oil contracting and negotiations. The MoO participants' questions showed active interest and listening, but also a low level of general knowledge in the areas of their job responsibilities. The MoO personnel generally spoke freely about their current contracting efforts and issues they have faced in their work. This cable contains market sensitive information, please protect accordingly. End Summary

Contracting Officers Needed: Experience not Necessary

¶2. (C) The contracting terms and ideas introduced in the course would not challenge those with more than a passing knowledge of the subject matter. For example, the Iraqi participants generally were unfamiliar with the basic terminology used in oil contracting, "R factor," describing the ratio between company costs and revenues. The participants also exhibited a poor understanding of the role of arbitration in disputes. Their questions showed a greater comfort level with taking disputes to court rather than arbitration. They had no knowledge of major bodies that conduct arbitration like the International Chamber of Commerce. The Iraqis recognized their deficiencies in most cases and were eager to improve their knowledge.

They're Coming to Steal our Oil

¶3. (C) The Iraqi participants also showed distrust for outside actors. The subject of "booking reserves" was brought up and the MoO delegation reacted strongly against the idea. They believed that when a company booked Iraqi oil reserves, the company was claiming ownership to the oil in the ground. The Iraqi participants rejected explanations that the concept is mainly an accounting issue and could help Iraq to attract valuable contracting bids. Later, in one-on-one conversations with Econoff, the Iraqis remained mystified by the concept, but they did seem more willing to explore the idea. Dr. Sabah said that Iraq should join the New York Convention on the Enforcement of Arbitral Awards because it would be good for Iraq to attract investors. He recognized the Convention's benefits, but he also identified arbitration in a third country as an IOC stratagem to gain an unfair contractual advantage over Iraq.

Opinions on Oil Production Contracts

14. (C) Outside the actual course work, the Iraqis discussed current contracting efforts. The group repeatedly asked what type of production contract was best. As a group, they remarked that international media overstated and perpetuated the negative security situation in Iraq. They believed that the IOCs would otherwise be eager to enter Iraq because of the IOCs would otherwise be eager to enter Iraq because of its huge reserves and the ease of production from the Iraqi reservoirs. In contrast to recent announcements by Oil Minister Shahrastani, Dr. Sabah said that Iraq would allow risk service contracts for the exploration blocks and not resort to production sharing agreements. They also commented that, in addition to the revival of a Saddam-era contract signed with CNPC for the Ahdab field, the MoO was conducting negotiations with Petrovietnam for the Amara field, another Saddam-era PSC contract.

Discussion of the Bid Rounds

15. (C) The group also talked about issues directly related to the first and second bid rounds. They said that the contract had only three biddable parameters; Production Target, Incremental Remuneration Fee, and the Baseline Production Rate. (Comment: This seemed to be at odds with the original contract and its articles, but points to a heavy emphasis on the financials of the contract rather than the technical side. It ignored the minimum work requirement, Iraqi on-the-job training or "local content", and budgeting training for Iraqi personnel, all included in the written contract. End Comment.) Mr. Basim Ibraheem Dawood, a petroleum engineer of the Field Development Directorate,

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expressed a concern about the oil recovery factor, the percentage of oil actually produced from the field over its lifespan. He noted that oil is an asset for all Iraqis and their children. His concern demonstrated that some Iraqis prefer to contract with an IOC with the technical capability to produce as much oil as possible, and not simply to increase production as quickly and cheaply as possible.

Bid Round Management Structures

16. (C) In reference to the brown fields, i.e., developed fields, offered in the first round, Dr. Sabah said that the operating company currently working the field would create a Field Operating Division (FOD). The FOD would continue to manage the field while the IOC would submit its work plan to the FOD for approval. The FOD would have the final say in what work would be done, not the IOC. In lesser developed or undeveloped "green" fields and the new gas fields, the Iraqis would form a Joint Management Company (JMC) to manage the fields. This would differ from the JMC in that, as a group, the IOC and the Iraqi operating company would create a work plan by consensus. The Iraqi training participants said that, unlike normal contracting practice to encourage transparency, the bid parameter evaluation criteria were proprietary to the MoO.

Oil Experts Express Concerns

17. (C) In private discussions, the expert trainers and Econoff agreed about several areas of concern. On the MoO's EPC contracts, the experts said that the IOCs would view them as loss leaders and not the type of contract they would normally enter into. They also said that the terms of the model contracts in the first and second bid round seemed very unattractive. They noted that the model contract terms called for the use of "state of the art" technology and not the best technology for the particular field, which could be problematic when the IOCs present their work plans. The experts uniformly opined that a Western company and not the Iraqis had written the contract, since it addressed all the right issues and said all the right things. The particulars

of the contract, however, clearly had a heavy Iraqi hand, which the experts did not believe had been for the better.

Comment: More Training Needed

18. (C) Overall, the team the Iraqis sent to Jordan seemed eager to learn, but lacked the experience and knowledge needed to fully engage the IOCs in negotiations. Certain members showed strengths in their individual technical fields as accountants, lawyers and geologists, but lacked base knowledge in international contracting. With further training the team can become the nucleus for an excellent contracting department in the MoO. Time may not allow them to develop the needed skills, however, before the bulk of the Iraqi oil production contracts are completed. This could present difficulties both for the MoO as it struggles to complete the bid rounds according to a shortened and ambitious timetable and for the IOCs as they work to finalize contracts and make the investments that Iraq's petroleum sector so desperately needs. We recommend the USG and other donors continue to find ways to increase MoO's capacity to develop its petroleum resources for the good of the Iraqi people.
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